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No. 87-543

In the Supreme Court

OF THE

United States

OCTOBER TERM, 1987

TRANSWESTERN PIPELINE COMPANY,
Petitioner,

VS.

FEDERAL ENERGY REGULATORY COMMISSION,
Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

BRIEF OF RESPONDENT SOUTHERN CALIFORNIA GAS COMPANY IN OPPOSITION TO PETITIONER

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November 4, 1987

QUESTIONS PRESENTED

1. Whether the Federal Energy Regulatory Commission (Commission) reasonably exercised its statutory authority to regulate a natural gas pipeline company's rates by eliminating from its tariffs "minimum bill provisions" which it had found to be unjust and unreasonable.

2. Whether the Commission's finding that the minimum bill provisions in the pipeline's tariffs have anticompetitive effects was supported by substantial evidence.

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LIST OF PARENT, SUBSIDIARIES AND AFFILIATES

Southern California Gas Company (SoCalGas) is a wholly-owned subsidiary of Pacific Lighting Corporation. The following are the parent, subsidiaries and affiliates of SoCalGas:

American Diversified Sports, Inc.
Central Plants, Inc.
Colorado Wholesale Sporting Goods Co.
Dual Fuel Systems, Inc.
8309 Tujunga Avenue Corp.
FTM Sports Corporation
Gart Bros. Sporting Goods Company
Mayflower Realty Associates, Inc.
Michigan Sporting Goods Distributors, Inc.
Modular Products, Inc.
Pacific Center Downtown, Inc.
Pacific Energy Resources Incorporated
Pacific Enterprises
Pacific Gas Gathering Company
Pacific Geothermal Company
Pacific Hydropower Company
Pacific Indonesia LNG Company
Pacific Interstate Company
Pacific Interstate Mojave Company
Pacific Interstate Offshore Company
Pacific Interstate Transmission Company
Pacific Interstate Transmission Company (Arctic)
Pacific Library Tower
Pacific Lighting Bio-Energy Company
Pacific Lighting Capital Company N.V.
Pacific Lighting Commercial Loans, Inc.
Pacific Lighting Corporation
Pacific Lighting Energy Systems
Pacific Lighting Exploration Company
Pacific Lighting Gas Development Company
Pacific Lighting International Finance N.V.
Pacific Lighting Land Company
Pacific Lighting Leasing Company

Pacific Lighting Oil and Gas Company
Pacific Lighting Overseas Finance N.V.
Pacific Lighting Real Estate Group
Pacific Offshore Pipeline Company
Pacific Oroville Power, Inc.
Pacific Penobscot Power Company
Pacific Recovery Corporation
Pacific Synthetic Fuel Company
Pacific Western Resources Company
Pacific Wood Fuels Company
Presley ASW Finance Co., Inc.
Presley Financial Corporation
Presley-Home Mac Finance Co., Inc.
Presley RAC Finance Co., Inc.
Rexall Square Drugs, Inc.
Sabagli N.V.
Southern California Conservation Financing Company
Southern California Gas International Finance N.V.
Southern California Gas Tower
Southern California Tower
Sports Castle Travels, Inc.
Terra Resources, Inc.
Thrifty Corporation
Thrifty Jr. Inc.
Thrifty Realty Company
Thrifty Wilshire Inc.
United Merchandising Corp.
Western Power, Inc.

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On Petition for a Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

BRIEF OF RESPONDENT SOUTHERN CALIFORNIA GAS COMPANY IN OPPOSITION TO PETITIONER

Respondent, Southern California Gas Company (SoCalGas),[1] respectfully requests that this Court deny the Petition for Writ of Certiorari seeking review of the opinion of the United States Court of Appeals for the

[1]SoCalGas and its affiliate, Pacific Lighting Gas Supply Company (PLGS) were parties in the proceeding before the Federal Energy Regulatory Commission. Recently, SoCalGas and PLGS merged and are operating under the name of SoCalGas.

Fifth Circuit in this case. App. at A-1.[2] This case does not merit this Court's review. Petitioner, Transwestern Pipeline Company (Transwestern), has had an opportunity for a full and fair hearing. It has been unable to convince either the Federal Energy Regulatory Commission (Commission) or the Court below of its arguments. This is not a case in which there is any conflict among the Circuits and Transwestern has not cited to any. In fact, the Fifth Circuit Court of Appeals' decision in this case is completely consistent with a similar recent decision of the District of Columbia Circuit Court of Appeals in *Wisconsin Gas Company v. FERC.*, 770 F.2d 1144 (D.C. Cir. 1985), *cert. denied sub nom., Transwestern Pipeline Company v. FERC*, 106 S. Ct. 1968 (1986) and 106 S. Ct. 1969 (1986). There is no issue of Constitutional or national interest raised by the Petitioner. This case involves no significant issue concerning the administration of the Natural Gas Act. 15 U.S.C. § 717-717w (1982). The issues in this case involve matters of settled law which were properly applied by the Commission and the Court below.

STATEMENT OF THE CASE

This case involves the Commission's elimination of a provision in a natural gas pipeline's tariff known as a "fixed cost minimum bill". The fixed cost minimum bill is a tariff provision which requires the pipeline's customers to pay the pipeline the fixed costs associated with its service including the pipeline's return on equity (profit) and related income taxes regardless of the volume of gas purchased by the pipeline's customers. In its place the Commission authorized the use of a cost recovery method-

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[2]The appendix references are to the appendix filed with this Court by Transwestern Pipeline Company.

ology known as the modified fixed variable rate design (mfv). Under this methodology, debt and virtually all other fixed costs are collected from customers in a fixed charge such that only gas costs and costs related to the pipeline's profit and certain other relatively minor costs are collected from the customers dependent upon the volume of gas sold or transported.

In Order No. 380,[3] the Commission eliminated minimum commodity bills in the tariffs of interstate pipeline companies to the extent these provisions permitted the recovery of nonincurred variable costs. The question of the continuing validity of the fixed cost portion of minimum bills was left to be resolved in individual pipeline proceedings. This present case is such a proceeding. Based upon the unique facts and circumstances which existed in this case, the Commission's decision eliminated the fixed cost portion of the minimum bill.

Transwestern is an interstate pipeline company subject to the jurisdiction of the Federal Energy Regulatory Commission under the Natural Gas Act. It provides firm natural gas sales and transportation services to essentially two customers, SoCalGas and Northwest Central

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[3]Order No. 380 [1982-1985 Regulation Preambles Transfer Binder] FERC Statutes and Regulations ¶ 30,571 (1984); Order No. 380-A, [1982-1985 Regulation Preambles Transfer Binder] FERC Statutes and Regulations ¶ 30,584 (1984); *Elimination of Variable Costs from Certain Natural Gas Pipeline Minimum Commodity Bill Provisions*, Order No. 380-B, 29 FERC ¶ 61,076 (1984); Order No. 380-C, [1982-1985 Regulation Preambles Transfer Binder] FERC Statutes and Regulations ¶ 30,607 (1984); *Elimination of Variable Costs from Certain Natural Gas Pipeline Minimum Commodity Bill Provisions*, Order No. 380-D, 29 FERC ¶ 61,332 (1984), *aff'd sub nom. Wisconsin Gas Company v. FERC*, 770 F.2d 1144 (D.C. Cir. 1985), *cert. denied sub nom., Transwestern Pipeline Company v. FERC*, 106 S. Ct. 1968 (1986) and 106 S.Ct. 1969 (1986).

Pipeline Corporation (Northwest Central).[4] SoCalGas is a natural gas distribution company which provides natural gas service in southern and central California. SoCalGas has more than 4 million customers and provides natural gas service to a population of approximately 13 million. It purchases natural gas from a number of other interstate pipeline companies including El Paso Natural Gas Company (El Paso), and three affiliates, Pacific Interstate Transmission Company, Pacific Offshore Pipeline Company and Pacific Interstate Offshore Company. Northwest Central is an interstate pipeline company which sells gas primarily to local distribution companies in the Midwest. It also purchases natural gas supplies from sources other than Transwestern.

In 1959 the Federal Power Commission (FPC) issued a certificate of public convenience and necessity under Section 7 of the Natural Gas Act, 15 U.S.C. § 717f (1982), to Transwestern for service to SoCalGas. *Transwestern Pipeline Company,* 22 FPC 391 (1959), *Order on Rehearing,* 22 FPC 542 (1959). In the Commission's Order on Rehearing in the Transwestern original certificate proceeding, the FPC established Transwestern's minimum bill with SoCalGas at a 91% level for two reasons. First, the 91% level was found necessary for financing of the new pipeline and, second, the 91% minimum bill level was the same as that provided to El Paso which served the same market. *Id.* 22 FPC at 543.

During the 1960's, Transwestern's system was expanded. Transwestern's service to SoCalGas was increased to 750 million cubic feet per day (MMcf/d). The

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[4]Northwest Central has been renamed as Williams Pipeline Company. In this brief it will be referred to as Northwest Central.

tariff still provided for a 91% minimum annual bill. During this period, Transwestern added a second customer, the predecessor of Northwest Central. Subsequently, Transwestern's service to Northwest Central was increased to 250 MMcf/d.

Both SoCalGas and Northwest Central are partial requirement customers of Transwestern. Both are entitled to receive firm contract demand service, and yet both were curtailed severely during the 1970's. This curtailment reached its greatest point in 1978 when Transwestern was only able to supply approximately 60% of its contract demand quantity. Yet the effect of this curtailment on the minimum bills of each company was vastly different. SoCalGas's minimum bill did not change. However, there are provisions in the Transwestern service agreement with Northwest Central which resulted in the reduction of Northwest Central's minimum bill obligation because of curtailment. As a result, while SoCalGas's minimum bill remained at the 91% level, Northwest Central's minimum bill was reduced to 59% of its annual contract demand.

On August 28, 1981, Transwestern tendered for filing proposed changes on its tariff under Section 4 of the Natural Gas Act. The Commission initiated hearings under Sections 4 and 5 of the Natural Gas Act, *inter alia*, on the lawfulness of Transwestern's minimum bills and rate design methodology. Extensive hearings were conducted on the issue of Transwestern's minimum bill, rate design and other matters. During this hearing a number of parties proposed and advocated the complete elimination of both fixed cost and variable cost minimum bills.

After the close of hearings, the Transwestern proceeding was consolidated with other cases concerning an investigation under Section 5 of the Natural Gas Act, 15

U.S.C. § 717d (1982), of the minimum bills of other interstate pipelines which supply gas to California. *Pacific Gas Transmission Company,* 25 FERC ¶ 63,062 (1983), 25 FERC ¶ 63,079 (1983), *aff'd.*, 26 FERC ¶ 61,111 (1984), *reh'g denied*, 27 FERC ¶ 61,003 (1984). Prior to any hearing on the consolidated dockets, the Commission suspended the consolidated proceeding and severed the Transwestern matter for decision. *Pacific Gas Transmission Company*, 28 FERC ¶ 61,217 (1984). Subsequently, the Commission terminated the investigation into the minimum bills of other pipelines serving California because the investigation had become moot with the elimination of nonincurred variable cost minimum bills by Order No. 380 and the Commission's decision therein to deal more efficiently with any remaining issues in the pipeline's individual proceedings. *Pacific Gas Transmission Company,* 32 FERC ¶ 61,001 (1985).

On December 11, 1984, the Presiding Administrative Law Judge (ALJ) issued his initial decision reducing Transwestern's fixed cost minimum bills. App. at E-1; *Transwestern Pipeline Company*, 29 FERC ¶ 63,054 (1984), *aff'd*, 32 FERC ¶ 61,009 (1985). The ALJ found that the differences between SoCalGas's and Northwest Central's minimum bills constituted undue discrimination. His proposed remedy to the Commission was to reduce Transwestern's minimum bill to the 60% level.

On July 1, 1985, the Commission in Opinion No. 238 affirmed, in part, the ALJ's initial decision, with modifications, including the complete elimination of Transwestern's fixed cost minimum bill. App. at C-1; *Transwestern Pipeline Company,* 32 FERC ¶ 61,009 (1985). Not only did the Commission find Transwestern's minimum bills to be discriminatory, it found that they unreasonably restrained trade and thus were unjust and unreasonable.

The Commission in Opinion No. 238-A denied rehearing. App. at D-1; *Transwestern Pipeline Company*, 36 FERC ¶ 61,175 (1986).

In its decisions, the Commission found that minimum bills were not justified, in part, because they forced SoCalGas and Northwest Central to purchase gas from Transwestern when lower cost alternative supplies were available. The Commission concluded that Transwestern's recovery of its fixed costs should not be risk free as was the case with its minimum bills. Instead, the Commission adopted a new rate design methodology which assured Transwestern of recovering most of its fixed costs, but placed at risk its return on equity and related taxes and some minor other costs. These limited fixed costs are recovered through the commodity charge. Thus, to the extent that Transwestern's services are price competitive its profits are increased.

The Fifth Circuit Court of Appeals affirmed the Commission's decision finding that the Commission's conclusions were based upon substantial evidence. The Court found the remedy imposed by the Commission was authorized under the Natural Gas Act and was not arbitrary or capricious. Finally, the court held that the Commission properly exercised its discretion in terminating its investigation into the tariffs of the other pipelines serving California and in determining the lawfulness of Transwestern's fixed cost minimum bill on the record before it.

REASONS WHY THE WRIT SHOULD BE DENIED

I

The Court's Decision Below Follows an Unbroken Line of Authority in Finding That The Commission Acted Within Its Authority to Modify Tariffs and Contracts Under Section 5 of The Natural Gas Act

Transwestern's attack upon the Commission's authority to modify contracts and tariffs under the Natural Gas Act is based upon a contorted and incorrect interpretation of the *Mobile-Sierra* doctrine and the cases thereunder. *United Gas Pipeline Company v. Mobile Gas Service Corporation*, 350 U.S. 332 (1956); *FPC v. Sierra Pacific Power Company*, 350 U.S. 348 (1956). The District of Columbia Circuit Court of Appeals in the *Wisconsin Gas v. FERC* case determined that the Commission's authority to act under Section 5 of the Natural Gas Act, 15 U.S.C. § 717d (1982), is so clear, and that virtually identical arguments by Transwestern were so tenuous such that Transwestern's assertions regarding the challenged Commission action were either "frivolous" or "completely without merit". *Id.* 770 F.2d at 1153.

Transwestern's reliance upon the *Mobile-Sierra* doctrine is misplaced. The *Mobile-Sierra* line of cases held that pipelines do not have the right under Sections 4 and 5 of the Natural Gas Act to unilaterally file to change their rates unless reserved by contract. *Mobile*, 350 U.S. at 340-41. However, even if a pipeline does not have the contractual right to file to change its rate, the Commission may change the rate when the rate is found to be contrary to the public interest. *Sierra*, 350 U.S. at 355. The Commission is given explicit authority to modify contracts in Section 5 of the Natural Gas Act. This authority is unchanged by *Mobile-Sierra*. This doctrine is

not a limitation but a confirmation of the Commission's authority. 15 U.S.C. § 717d.

Simply put, an argument cannot credibly be made that the Commission exceeded its authority in eliminating Transwestern's minimum bill provision. Section 5 of the Natural Gas Act empowers the Commission upon finding "that any rate, charge, or classification . . . or that any rule, regulation, practice or contract effecting such rate, charge or classification is unjust, unreasonable, unduly discriminatory or preferential" to determine the just and reasonable rate or contract and to fix the rate or contract to be thereafter observed by order. 15 U.S.C. § 717d(a). The court below recognized the Commission's authority when it stated "Section 5(a) provides the basis for the Commission's authority to examine rates to determine whether they comply with the § 4 standard . . ." that is, if the rate is just and reasonable. App. at A-8.

In fact, Transwestern acknowledges that the Commission is authorized under Section 5 of the Act to modify contracts and tariffs. *See* Transwestern's petition at p. 12. Transwestern cites no case which limits the Commission's authority to modify such tariffs or contracts. Instead, Transwestern argues that the Commission exceeded its authority because it did not fully consider the role of contracts under the Natural Gas Act. In essence, the arguments by Transwestern are merely disagreements with the Commission's weighing of the various factors which were considered in issuing its decision. The role of this Court is not to weigh the individual factors in evidence, but to defer to the expertise of the administrative agency in considering the evidence before it. *Permian Basin Area Rate Cases*, 390 U.S. 747 (1968), *reh'g denied*, 392 U.S. 917 (1968).

II

The Commission Has Engaged in Rational Decision-Making Which Has Been Affirmed by The Court Below

The Commission's finding that the minimum bills unreasonably restrained trade cannot be characterized as arbitrary and capricious. Transwestern does not deny that its minimum bills were not competitive. Instead, they argue that the Commission has improperly applied antitrust concepts in making its determinations under the Natural Gas Act.

In making this argument Transwestern misconstrues the standard the Commission applied and improperly applies the law. The Commission in its order did not enforce the antitrust laws. The Commission made its judgment under the Section 4 and 5 standards of the Natural Gas Act. While the Commission has looked at the body of antitrust law for guidance on promoting competition, it has not looked at a *per se* rule but rather an application of a rule of reason. *See Board of Trade of the City of Chicago v. U.S.*, 246 U.S. 231 (1918). As the Court stated, "Had the Commission simply determined that Transwestern's contracts with SoCalGas and Northwest restrained its customers' options to purchase gas from other suppliers, without more, we would be unable to approve the Commission's reasoning. The Commission did not, however, apply such a *per se* rule to eliminate Transwestern's minimum bill restraints." App. at A-13.

The Commission balanced the competitive harm caused by the minimum bills against the objectives of the minimum bills and the available alternatives. Based upon this analysis, the Commission concluded that on balance

Transwestern's minimum bills cause more harm than was warranted and, therefore, were unjust and unreasonable.

The Commission's order struck a reasonable balance between the promotion of competition and the expectation of investors to a fair return. The Commission's order provides Transwestern with a full and fair opportunity to recover its cost of service. Under the modified fixed variable rate design, Transwestern's rates incorporate a demand charge which recovers a significant portion of Transwestern's fixed cost. The determination of the proper mechanism under which a pipeline may recover its costs are matters properly left with the Commission. They are not matters which should be determined by the Court.

With this finding of anti-competitiveness the Commission was required to reject the minimum bill unless it filled a valid regulatory purpose. The Commission utilized the standard set forth in *Atlantic Seaboard Corporation*, 38 FPC 91 (1967), *aff'd. sub nom., Atlantic Seaboard Corp. v. FPC*, 404 F.2d 1268 (D.C. Cir. 1968), in order to determine if there was justification for a minimum bill.

After reviewing the relevant factors the Commission concluded that none of these factors justified a minimum bill for Transwestern. This review process is consistent with that applied by the courts. See *Mississippi River Transmission Corp. v. FERC*, 759 F.2d 945 (D.C. Cir. 1985); *Wisconsin Gas v. FERC*, 770 F.2d 1144 (D. C. Cir. 1985), *cert. denied sub nom., Transwestern Pipeline Co. v. FERC*, 106 S.Ct. 1968 (1986) and 106 S.Ct. 1969 (1986). Transwestern's argument that a different standard should be applied to it is without foundation and notably without citation.

Transwestern has argued that the Commission abused its discretion in not considering the minimum bills of

other pipelines serving California. This is not the case. The Commission's determination of the appropriateness of Transwestern's minimum bills was properly based upon the unique facts and circumstances of Transwestern. In affirming the Commission's decision, the Court below found "the possible competitive effect of the other pipelines' minimum bills cannot alter the determination that Transwestern's minimum bills had an adverse cost effect on its customers. This finding is supported by substantial evidence on the record." App. at A-33.

The Commission correctly exercised its broad discretion in fashioning its procedures in order to meet its responsibilities under the Natural Gas Act. In the exercise of this responsibility the Commission has been granted authority to manage the matters before it to ensure a reasonable and lawful decision. The Courts have consistently granted great deference to an agency in establishing procedures to accommodate the needs for administrative flexibility and economy. *Phillips Petroleum Company v. FPC*, 475 F.2d 842 (10th Cir. 1973); *Fort Pierce Utility Authority v. FPC*, 526 F.2d 993 (5th Cir. 1976); *Louisiana Power and Light Company v. FPC*, 526 F. 2d 898 (5th Cir. 1976); *Earth Resources Company v. FERC*, 617 F. 2d 775 (D.C. Cir. 1980). The rule that a federal agency has the authority to fashion procedures to manage the cases before it is so well established that there is no need for this Court to review this matter.

III

The Court's Decision Below Gave Full Consideration to the Issues Before It and Determined That The Commission's Decision Was Based Upon Substantial Evidence

The Court of Appeals' decision in this case demonstrates a thorough analysis of the issues and conclusively affirms that the Commission's decision was supported by substantial evidence. App. at A-22. Transwestern's basic argument is that the record does not contain evidence on Transwestern's fixed cost minimum bill because the Commission issued Order No. 380, which eliminated variable cost minimum bills, after the record was closed. It is clear that the question whether a full cost minimum bill should be eliminated encompasses the question whether a fixed cost minimum bill should also be eliminated. These issues were presented to the Commission through the hearing process before the record was closed. As the Court below found, "Transwestern had a full, fair opportunity to present evidence on the lawfulness of the fixed cost minimum bills." App. at A-22. Under these circumstances Transwestern's claims simply do not merit review by this Court.

Pursuant to Section 19(b) of the Natural Gas Act, 15 U.S.C. § 717(b), the standard which is to be used by a Court in reviewing the Commission's factual findings is that of substantial evidence. *Public Service Commission of the State of New York v. FERC*, 642 F. 2d 1335 (D.C. Cir. 1980), *cert. denied*, 454 U.S. 879 (1981) and *cert. denied*, 454 U.S. 880 (1981). The factual findings of the Commission are to be considered conclusive if supported by substantial evidence. In this regard the Court is not to substitute its view of the facts for that of the Commission. *Colorado Interstate Gas Company v. FPC*, 142 F. 2d 943

(10th Cir. 1944), *aff'd.*, 324 U.S. 581 (1945), *reh'g denied*, 325 U. S. 891 (1945). This Court has repeatedly stated that it is the primary responsibility of the Court of Appeals to determine whether an agency's decision is supported by substantial evidence and this Court will only intervene when the standard has been misapprehended or grossly applied. *American Textile Manufacturers Institute v. Donovan*, 452 U. S. 490 (1981); *Mobil Oil Corporation v. FPC*, 417 U.S. 283 (1974). They have not been misapprehended or grossly applied in this case.

IV

The Commission Fully Considered the Impact of Take or Pay Obligations in Making Its Decision

Contrary to Transwestern's assertions, the Commission in its decision considered the impact of the elimination of Transwestern's minimum bill on potential take or pay payments by Transwestern. The Commission found that there is no connection between the minimum bill payments of the customer and the cost of potential take or pay liability. There was no evidence in the record that Transwestern will incur substantial take or pay liability solely because of elimination of its minimum bills. The evidence demonstrated that SoCalGas would purchase significant volumes of gas from Transwestern as long as Transwestern's gas is marketable. As the Court below noted, Transwestern has acknowledged that the Commission is instituting alternative approaches to the industry wide take or pay problem. App. at A-20. As the Court stated,

> The take or pay issue posed here is a separate matter which is being addressed in other proceedings before the Commission and through other means.
>
> . . .

> The Commission's decision to confront the potential take or pay problem through alternative approaches and in other cases has not been shown to be unreasonable, arbitrary or capricious.

App. at A-20.

Further, Transwestern fails to state that even if it makes take or pay payments, the Commission's regulations provide for the recovery of the carrying costs of such payments. Account No. 165 of the uniform system of accounts permits Transwestern to book take or pay payments as a rate base item, and upon successful application to the Commission, it may earn a return on the payments. 18 C.F.R. § 201. Therefore, even if Transwestern incurs take or pay payments, the carrying costs of such payments could be recovered in Transwestern rates. Further, the Commission is attempting to deal with the take or pay issue in response to the District of Columbia Circuit Court of Appeals' opinion in *Associated Gas Distributors v. FERC*, 824 F.2d 981 (D.C. Cir. 1987). See, Order No. 500, 40 FERC ¶ 61,172 (1987). It should be noted that there is no evidence on the size or likelihood of any take or pay payments. The Court below characterized this question as "a hypothetical issue". App. at A-20.

With the lack of any evidence on the link, if any, between Transwestern's fixed cost minimum bills and the incurrence of take or pay payments, and with the various alternatives available to Transwestern and with the uncertainty of any take or pay payments, it was not arbitrary or capricious for the Commission to eliminate Transwestern's minimum bills. Transwestern's arguments, which are nothing more than a disagreement with a factual finding of the Commission, do not warrant Court review.

CONCLUSION

For these reasons, the petition for a writ of certiorari should be denied.

Respectfully submitted,

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November 4, 1987